Repeal Deficit Reduction Fuel Taxes

AAR supports S. 820 and H.R. 1001 that would repeal deficit reduction fuel taxes paid by railroads and barges. AAR opposes H.R. 2060 that would create a railroad trust fund from deficit reduction fuel taxes.

Inequitable Taxation in a Surplus Environment

The railroad and inland barge industries pay a 4.3 cents per gallon deficit reduction fuel tax even though there is no longer a federal deficit. Furthermore, the railroad and inland barge industries are required to pay deficit reduction fuel taxes while their competitors, the truckers, do not.

Among all U.S. industries, only transportation industries have been obligated to pay special deficit reduction fuel taxes, and today, among the different transportation modes, only railroad and barge companies continue to pay such a tax. The deficit reduction fuel tax rate has varied over time, and currently stands at 4.3 cents per gallon on diesel fuel consumed. Since inception of the tax in 1990, freight railroads have paid over $1.4 billion in deficit reduction fuel taxes. Railroads continue to pay these taxes even though there is no longer a federal deficit.

Trucking companies, direct competitors of railroads and barge companies, do not pay a deficit reduction fuel tax. The entire revenue from the taxes paid by the truckers is paid into the Highway Trust Fund, and is used to pay for improvements and maintenance of highway infrastructure. Therefore, while railroads continue to contribute to a non-existent deficit, the truckers contribute to their own infrastructure improvement.

By contrast, the railroad industry does not have a trust fund but privately funds its own maintained rights-of-way. In 1998, freight railroads spent $7.7 billion maintaining and improving their own infrastructure. This is equivalent to a tax of $2.13 per gallon of fuel consumed by railway locomotives — an amount, which is four to ten times the equivalent of tax paid by the competing modes of transportation.

Both the House and Senate 1999 tax cut bills, acknowledged the tax inequity and included a repeal of the 4.3 cent deficit reduction fuel tax for the railroad and barge
industries, but the final 1999 tax cut bill was vetoed by President Clinton for reasons other than the railroad tax repeal.

Support for an Equitable Solution

The railroads are not alone in calling for a fair and equitable solution to the current deficit reduction fuel tax problem. The U.S. Chamber of Commerce and the American Road and Transportation Builders Association (ARTBA) have adopted policies in support of repealing the 4.3-cent deficit reduction fuel tax. Numerous agriculture groups including the American Farm Bureau Federation, American Soybean Association, National Association of Wheat Growers, and the National Corn Growers Association are also on record supporting the repeal of this tax.

Railroad Trust Fund Proposals

AAR opposes H.R. 2060, the Railway Safety and Funding Equity Act of 1999 (RSAF), a bill that would transfer the 4.3-cent deficit reduction fuel tax into a new Railroad Trust Fund for highway-rail grade crossing safety programs. H.R. 2060 would divert significant railroad resources to help solve what is fundamentally a highway safety problem. Not only is this proposed cross subsidy of highway needs by the railroads bad public policy, but these railroad fuel tax revenues are needed to meet significant railroad infrastructure needs.

AAR also opposes any effort to use the 4.3 cents per gallon deficit reduction fuel tax paid by the railroads to create a Railroad Trust Fund to finance short-line/regional railroad improvements, intercity or commuter passenger rail needs, or other purposes. In these scenarios, the beneficiaries of the funds, while having contributed little or nothing, would profit from a cross-subsidy from the large freight railroads. It is not appropriate to expect the large railroads to provide additional funding support for passenger rail, short-lines, or highway-rail traffic control devices. Neither do large railroads care to finance their own infrastructure needs through a Railroad Trust Fund by inefficiently sending funds to Washington, DC, simply to be returned to private sector railroads, minus bureaucratic administrative and overhead costs, and subject to political manipulation and government regulatory red tape.

Summary

The railroads' true advantage in cost, environmental impact, reduced highway damage and congestion, safety, and fuel efficiency rightfully have become important criteria in a modal choice. Artificial cost barriers to the use of freight transportation, in terms of inequitable deficit-reduction taxes, can only disadvantage rail in the competitive marketplace and distort consumer choice.

2256
The Importance of Fuel Diversity in Establishing a National Energy Policy and a Sound Climate Change Strategy

The U.S. economy is highly dependent on affordable electricity. Since 1970, electricity growth has closely tracked the rise in GDP. To meet increased demand and to offset retirements of existing power plants, the Department of Energy forecasts that 1,310 new power plants – with 393 gigawatts of capacity – will be needed by 2020. A sound national energy policy is needed to continue to ensure the affordability and reliability of electricity, and to meet future energy demands.

The Coal-Based Generation Stakeholders (CBGS) group believes that fuel diversity – coal, natural gas, nuclear energy, oil, hydropower and other renewables, to generate electricity – must be maintained as a matter of national energy policy and national security. An energy policy that maintains fuel diversity can appropriately balance continued utilization of coal, the most essential fuel for reliable and affordable electricity, with a sensitivity to the climate change issue that reflects both economic and environmental objectives.

The industries that comprise CBGS have long supported voluntary, flexible, cost-effective and inclusive approaches to reducing greenhouse gases. For example, under the Climate Challenge program, the electric utility industry was projected to reduce 174 million metric tons of carbon dioxide (CO₂)-equivalent greenhouse gases in 2000. The electric power industry is currently developing a voluntary climate initiative that would serve as an extension of the Climate Challenge program. The industry expects to partner with the federal government – particularly the Department of Energy – and other industries to pursue approaches to further reducing greenhouse gases. This initiative will reduce greenhouse gases in the near term, and promote a technology research, development and deployment (R, D & D) program that will lead to the development of cost-effective options to reduce greenhouse gases.

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2 Coal-based generation is increasingly clean. Since 1970, coal-based electric generation has increased 234 percent and coal use in power plants has increased 270 percent, yet criteria pollutant emissions have steadily declined. EIA, “Annual Energy Review 1999.”
3 “Voluntary” recognizes that the climate change issue merits policy responses that explore economically sustainable measures should any legally binding agreement to address greenhouse gases be adopted. Full “flexibility” encompasses emissions trading, project-based offsets, forestry and soils projects, and banking, which will be critical in the event of any domestic or international agreement. “Inclusive” encompasses all greenhouse gases; all sources and sinks; and all locations, domestic and international.
4 “Reduce” means reduce, avoid, sequester or otherwise mitigate greenhouse gases, whether domestically or internationally.
CBGS supports continued scientific research to evaluate if human activity is adversely affecting the climate, and, if so, to evaluate the causes, costs, policies and adaptation strategies to address possible solutions. Consistent with the President's March 13 letter to several Senators, CBGS opposes ratification of the Kyoto Protocol because it would cause serious harm to the U.S. economy and lacks binding commitments for all nations. Also consistent with the President's letter, CBGS strongly opposes regulation of CO₂ or any other greenhouse gas as a pollutant under the Clean Air Act or other legislation.

Because there is currently no cost-effective control technology for greenhouse gas emissions, compliance with stringent, mandatory targets and timetables such as those contained in the Protocol would cause massive fuel switching in the electric utility industry from coal to natural gas,⁴ which would be enormously expensive and dramatically increase electricity prices,⁵ and which would further exacerbate the fuel diversity issue. A Kyoto Protocol-type scenario would also raise serious problems in natural gas supply, prices and infrastructure, and would cause significant job losses in CBGS industries and among our suppliers. Stringent targets and timetables other than those contained in the Protocol also could be harmful to our nation's economy and energy policies. Moreover, they could have a chilling effect on badly needed investment in new coal-based generation because of a legitimate concern that such investments would become stranded in the event legally binding regulations were imposed in the future.

As currently envisioned, a sound voluntary climate initiative would consist of three major elements:

1. In the short term, the climate initiative is expected to achieve credible, verifiable emission reductions or offsets of greenhouse gases facilitated by certain policies and incentives from the federal government, including those that encourage full flexibility for emission credit and trading programs.

2. Further reductions of greenhouse gases in the medium to long term would result from the development and application of more energy-efficient, cost-effective electricity supply options, such as clean coal technology and renewables, that allow for a reliable and affordable supply of energy.

⁴ See, e.g., the reference study that demonstrates that under a Kyoto Protocol-type scenario, coal would decline from 50 percent of electric generation to as low as 13 percent in 2010, while natural gas would rise from 25 percent to 50 percent in the same time frame. Research Data International, Inc., U.S. Gas and Power Supply under the Kyoto Protocol, Vol. 1 at 1-9 (Sept. 1999).

⁵ A recent EIA report (which actually understates costs because mercury has not yet been analyzed) found that reductions in sulfur dioxide, nitrogen oxides and CO₂ consistent with recent legislative proposals would increase electricity prices by 17-33 percent in 2005, and by 50-43 percent in 2010. EIA, Analysis of Strategies for Reducing Multiple Emissions from Power Plants: Sulfur Dioxide, Nitrogen Oxides and Carbon Dioxide xvii, 27 (Dec. 2000). The bulk of the cost increases are due to CO₂ restrictions.
3. A climate technology R, D & D program is needed to ensure that cost-effective technologies are developed in the long term. This program should complement overall U.S. energy policy and the Framework Convention on Climate Change.

- In accordance with legislation introduced in the 106th Congress – such as S. 882, S. 1776, S. 1777 and S. 3253 – and public-private studies, the R, D & D program could focus on 1) advanced technologies in electric generation and transportation, 2) cost-effective direct carbon capture and removal from powerplant and other emission sources, and 3) carbon sequestration in natural “sinks” such as forests, soils and oceans.

- Two program goals could be to 1) fast track such climate technologies to market, and 2) promote export of such technologies overseas, particularly to developing countries such as China and India that could greatly benefit from more energy-efficient electric generation technology.

- In partnership with the federal government, the climate initiative would be expected to adequately fund the climate technology R, D & D program and to provide appropriate financial incentives, with periodic reassessment. Industry partners that install new climate technologies would be interested in recouping any substantial investments over a reasonable period of time.

The climate initiative should be consistent with government policies that encourage full flexibility, both domestically and internationally, in emissions trading, project-based offsets, forestry and soils projects, and banking. Financial and policy-oriented government incentives should be explored as a means to jump start credit and trading programs, offset projects, and the climate technology program.

Development of a voluntary climate initiative presents an opportunity not only for innovative emission reduction programs, but also for the inclusion of a broader number of partners involved in the life cycle of coal-based generation. For example, credit could be given to environmental improvements from extracting coal at the mine and delivering it to the generator.

CBGS believes that a climate change strategy premised on a voluntary climate initiative would achieve both environmental and economic objectives, and would help maintain fuel diversity. The strategy would reduce greenhouse gases in the short term as technological responses are developed for long-term availability, all the while maintaining the viability of coal as a vital component of electric generation. In short, environmental policy would complement energy policy, which is consistent with the President’s goal of ensuring that global climate change issues are addressed “in the context of a national energy policy that protects our environment, consumers, and economy.”

* See, e.g., Battelle’s Global Energy Technology Strategy – Addressing Climate Change (2000).
New Source Review

Description: The Clean Air Act imposes stringent "new source" control technology requirements on new units, and on existing sources if they are extensively modified. In 1996, EPA reinterpreted the new source review (NSR) program in a way that redefines when an existing source is considered to have been "modified," and issued a proposed rule consistent with this reinterpretation. EPA's approach presents an obstacle to efficiency improvement projects, safe operations and reliable generation, which is inconsistent with a sound national energy policy and the need to continue to ensure affordable and reliable electricity.

In addition, EPA has initiated litigation against over 40 investor owned power plants and 10 TVA plants to force installation of new control technology on plants that EPA alleges have been modified. EPA's litigation and enforcement strategy is inconsistent with past interpretations and implementation of the NSR program.

Status: EPA has not yet finalized its proposed NSR rule, but, on December 12, 2000, the agency published a Federal Register notice regarding a Detroit Edison project that has national implications because it interprets the existing NSR rule to cover reliability and efficiency improvement projects. In that notice, EPA claims, contrary to the language of the current NSR modification rules, that electric utility sources must get state (or EPA) approval before undertaking necessary maintenance, repair, and replacement projects. An administrative petition has been filed requesting that the Administrator reconsider the Detroit Edison notice and confirm that EPA's 1992 WEPCo rule and pre-1996 policies remain in effect. Regarding ongoing EPA enforcement efforts, additional notices of violation and lawsuits are expected unless policy changes are initiated.

Key Issues/Decisions: How can the NSR program be reformed to complement national energy policy objectives, and to avoid being an impediment to efficient, safe and reliable plant operations?

Actions Requested: The Administrator should grant the Detroit Edison petition and publish notice of this action in the Federal Register. In that notice, EPA should confirm that the WEPCo rule and pre-1996 policies remain in effect pending a reevaluation of regulatory and policy options. The Administrator also should initiate true NSR reform. The industry is ready to work cooperatively with EPA on this effort.
Harmonizing Ozone Rules Under the Clean Air Act

Description: In January 2000, EPA issued its Clean Air Act “section 126” rule, requiring power plants and some industrial sources in 13 states to make significant cuts in nitrogen oxide (NO\textsubscript{x}) emissions to help four states (Connecticut, Massachusetts, New York and Pennsylvania, all of which filed petitions under section 126 requesting source-specific reductions) reduce their ozone levels. EPA insists targeted sources must comply by May 1, 2003, even though this date would make compliance very difficult because of the lead time needed to engineer, purchase, install and test emission control equipment. More importantly, this deadline conflicts with a court-ordered May 31, 2004 compliance date for EPA’s “SIP call” rule. The SIP call requires NO\textsubscript{x} reductions from power plants and some other sources in 22 eastern states, including those subject to the section 126 rule, and will necessitate capital costs in excess of $13 billion and associated O&M costs of at least this much. The North American Electric Reliability Council has issued a study concluding that pending NO\textsubscript{x} reductions will require many Midwestern coal-fired plants to retrofit with sophisticated new technologies, thus significantly increasing planned maintenance outages (on top of projected low reserves), and hence some reliability risks in the next several years. NO\textsubscript{x} controls are imminent, but it is imperative that reductions occur in the least burdensome and most economically responsible manner possible.

The section 126 rule also removes state flexibility to decide which sources to control and by how much. Many states want the section 126 rule deadline to be the same as the SIP call compliance date, or made inapplicable for states that implement the SIP call. Some northeast states, companies and environmental groups want the section 126 rule and its deadline retained. Congressional appropriators have repeatedly urged EPA to harmonize the section 126 rule and SIP call implementation dates.

Status: The Supreme Court denied an appeal by parties challenging the underlying merits of the SIP call rule; however, this did not affect the May 31, 2004 compliance date. Legal challenges to the section 126 rule are pending in the D.C. Circuit Court of Appeals. A decision is expected by spring 2001, but may not resolve the SIP call/section 126 conflict. In the interim, states face significant uncertainty in developing implementation plans. Similarly, regulatory certainty is critical to companies, yet affected sources currently do not know which deadline and what controls apply.

Key Issue/Decision: The section 126 and SIP call rules must be harmonized.

Actions Requested: Congress clearly intended that the SIP call process would drive state compliance with Clean Air Act emission reduction requirements. The section 126 rule explicitly provides the Administrator authority to deny, or withdraw prior approval of, any section 126 petition targeting sources in a state where EPA approves that particular state’s implementation plan. The Administrator should clarify immediately that the SIP call implementation schedule is controlling and that NO\textsubscript{x} reductions must be made by the May 31, 2004 compliance date.
Regulation of Mercury Emissions from Coal- and Oil-Based Power Plants

Description: On December 14, 2000, EPA made a “regulatory determination” under the Clean Air Act that regulation of mercury and possibly other hazardous air pollutants (HAPs) is “appropriate and necessary” for coal- and oil-based power plants. This decision automatically triggers a formal rulemaking, and EPA is scheduled to issue a proposed rule in late 2003 and a final rule in late 2004. EPA has estimated costs of a mercury control program to be about $5 billion annually, while DOE and others have estimated significantly higher costs. Members of Congress from both parties have raised concerns about the adverse consequences of mercury regulation, including impacts to the fish industry. A stringent mercury control program could impact fuel diversity and coal-based generation in the same manner as a mandatory CO₂ reduction program.

Unfortunately, the language of the regulatory determination could severely limit the Administrator’s future options. EPA’s designation of a specific regulatory approach — even though the regulatory determination is not a formal rule — means that new coal- and oil-based plants, as well as existing coal- and oil-based plants that are “reconstructed,” will be regulated immediately in accordance with the stringent, source-by-source control program called for in the determination. Ironically, this harsh impact occurs at the outset of a multi-year regulatory process during which EPA will be attempting to establish a scientific record that justifies a stringent mercury control rule. Note that a decision today to modify the regulatory determination would neither affect the regulatory schedule, nor hinder ongoing mercury-related health effects, fate-and-transport, and emission reduction technology research critical to making sound regulatory decisions.

Status: EPA’s regulatory determination was published in the Federal Register on December 20. The agency indicated it did not want more input on the determination, instead noting that a proposed rule will be subject to public review and comment. Legal challenges have been filed in the D.C. Circuit by the utility industry. An administrative Petition for Reconsideration also has been filed with EPA, in effect requesting the agency to withdraw that portion of the regulatory determination that prescribes a specific control program and immediately impacts new and reconstructed units.

Key Issues/Decisions: Electric utilities are explicitly treated differently under the CAA than other major sources of HAPs, in that EPA’s assessment of power plants “shall” address “alternative control strategies.” However, language in EPA’s determination sets in motion the regulation of mercury emissions under a strict, source-by-source control program that eliminates flexibility and use of market mechanisms. The Administrator should avoid this unnecessary limitation on possible regulatory options.

Actions Requested: The Administrator should (1) reconsider that portion of the regulatory determination that prescribes a specific control program and immediately impacts new and reconstructed units; (2) clarify that EPA does not intend to limit regulatory options when proposing a rule; and (3) clarify further that the regulatory determination applies only to mercury and not other HAPs.
AAR supports S. 820 and H.R. 1001 that would repeal the 4.3 cents per gallon deficit reduction fuel tax for the railroads and barges. This tax should be repealed because it is:

1. Discriminatory against railroads, since the trucking industry pays no deficit reduction fuel tax;

2. Economically unsound, because it artificially diverts traffic that otherwise would travel by rail; and

3. Inconsistent with national policy, because it violates the goals of economy, impartiality, energy efficiency, and environmental friendliness.

Additionally, large freight railroads oppose the transfer of these revenues to a federal Railroad Trust Fund or any other form of a transportation trust fund.
THE COAL MINE VALLEY FILL ISSUE

DESCRIPTION: In October 1999, a federal district court in West Virginia stunned the Nation's coal industry with a decision barring the longstanding practice of building valley and hollow fills to store the dirt and rock generated during coal mining. Bragg v. Robertson, 72 F. Supp. 2d 642 (S.D. W.Va. 1999), appeal pending. No. 99-2443 (4th Cir). Notwithstanding the fact that these engineered fill structures are both a necessary part of coal mining operations and expressly authorized by federal laws regulating coal mining, the court interpreted regulations issued under those laws as prohibiting their construction in hollows and valleys that inevitably contain stream courses. While the decision remains pending on appeal, the past Administration abandoned the working men and women of America's coal industry and announced that it now agreed with the court's view. The past Administration's action in this regard is not only contrary to the laws it administers, it will have economic consequences in West Virginia alone that a Marshall University study concluded will be "as great or greater than those of the Great Depression." Earlier in the same litigation, the federal agencies (EPA, OSM & COE) settled the claims related to the use of section 404 permits to authorize these fills under the Clean Water Act. The agencies agreed to conduct a programmatic Environmental Impact Statement which addresses environmental and economic consequences of different actions, as well as evaluate the better coordination of overlapping regulatory programs.

STATUS: The appeal in the 4th Circuit has been briefed and was argued on December 7, 2000. In the meantime, the EPA, OSM and COE are preparing a Draft EIS. EPA and COE also have pending a proposed rule published on April 20, 2000 clarifying that excess spoil is fill material subject to section 404 and not section 402 of the CWA. This rule would remove the ambiguity in the agencies' programs that the district court relied on to reach its erroneous conclusion that these fills as well as other activities that have the effect of replacing waters of the United States are not authorized by section 404.

KEY DECISIONS: Should any part or form of a Draft EIS be publicly released before the completion of the underlying technical, economic and other studies?

OPTIONS: * Delay public release of Draft EIS in any form until all the underlying studies are complete and have been subject to some form of peer review. This option is completely defensible and will assure that the EIS process on this matter will not be subject to criticisms related to its credibility and integrity.

* Allow the agencies to release an executive summary or other form of a draft EIS that purports to provide an overview of the current analysis of complex technical questions. This option will appease few and invite strong criticism from industry and, perhaps, the West Virginia state legislature that has funded part of the studies.

KEY DECISIONS: Whether EPA and COE should adopt as a final rule the proposal clarifying the scope of the section 404 program with respect to excess spoil and other activities that have the effect of replacing waters of the United States.

OPTIONS: * Proceed to adopt as final the proposed rule published on April 20, 2000. The rule is an important part of maintaining the integrity of the 404 program by clarifying a longstanding ambiguity that has caused grave uncertainty for the regulated community and the agencies. It not only addresses the excess spoil issue but other activities as well, e.g. landfills.

* Await the decision of the 4th Circuit to determine whether it would require any modification of the proposal to address the central features of the rule. At some point, the EIS on mountaintop mining will have to analyze how excess spoil fills are to be addressed within the prevailing regulatory schemes under the CWA and SMCRA and whether any conflicts exist.
Public-Private Fuel Efficiency and Emissions Partnerships

**What Should Be Done?** Establish a public-private partnership involving the federal government, railroads, and railroad suppliers designed to increase the fuel efficiency of, and reduce emissions from, diesel locomotives. The partnership should be similar to the "21st Century Truck Initiative" now underway.

**Why?** The partnership would encourage conservation of natural resources and reduced emissions by the nation's largest freight transportation provider. Moreover, the "21st Century Truck Initiative" will use hundreds of millions of dollars of federal funds to sharply increase fuel efficiency and lower emissions for motor carriers that compete against railroads. Equity demands that railroads receive the same support.

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**Issue Overview**

In April 2000, the Clinton Administration announced the creation of the "21st Century Truck Initiative," a public-private research partnership involving many of the nation's largest heavy-duty engine and truck companies; the U.S. Departments of Defense, Energy, and Transportation; and the Environmental Protection Agency.

The goals of the Truck Initiative include developing truck and bus technologies that increase fuel economy, improve safety, reduce emissions, and lower costs. The partnership is designed to lead, within 10 years, to prototypes that double existing fuel economy for long-haul trucks and significantly reduce truck emissions of nitrous oxide, particulates, and other air pollutants.

Because of the Truck Initiative, the fiscal year 2001 budget saw an increase of $31 million in truck research spending to a total of $137 million.

Railroads account for more than 40 percent of the nation's freight ton-miles, considerably more than trucks' 29 percent share. Therefore, increases in rail fuel efficiency would significantly benefit our economy and environment. However, there is no public-private program involving railroad locomotives similar to the Truck Initiative. Instead, railroads and their suppliers must fund research and development efforts aimed at increasing fuel efficiency and reducing emissions on their own. For example, the Burlington Northern and Santa Fe Railway and the Union Pacific Railroad are spending more than $1 million apiece on these issues, while the Association of American Railroads is funding an industry-wide emissions research program.
A federal program to increase fuel efficiency and reduce emissions from diesel locomotives will provide public benefits to the environment similar to those of the 21st Century Truck Initiative.

By providing motor carriers a major federal subsidy through the Truck Initiative, the federal government will artificially reduce motor carrier costs. This imbalance between trucks and railroads will encourage shippers to use trucks, even where railroads provide more efficient services.

The U.S. Department of Transportation's Moving America: New Directions, New Opportunities - A Statement of National Transportation Policy notes that "Federal programs and policies must treat modes and carriers fairly." This condition is clearly violated if motor carriers receive federal benefits not made available to their competitors.

A federal program will magnify the substantial strides in both fuel efficiency and emissions control already accomplished by the railroads. Railroad fuel efficiency is up 16 percent since 1990 and 58 percent since 1980. Railroads are also committed to substantial reductions in atmospheric emissions, having endorsed an EPA proposal that calls for a 60 percent reduction in nitrogen oxide emissions from locomotives manufactured beginning in 2005. With federal support, the railroad industry can build on its own voluntary achievements and foster improved conservation and emissions control.

![Graph showing Revenue Ton-Miles Per Gallon of Fuel Used from 1981 to 1998](image)

Source: AAR
March 15, 2001

Vice President Richard B. Cheney
The White House
Washington, DC 20500

Dear Mr. Vice President:

We are addressing this letter to you in your capacity as chairman of the White House Energy Policy Development Task Force. We co-chair the Coal-Based Generation Stakeholders Group, an informal coalition of utilities, coal producers and railroads whose companies represent nearly one million employees and $275 billion in combined revenues. The coalition is working together to promote a balanced energy policy that recognizes the critical role coal-based electric generation plays in America's national and economic security.

We applaud the announcement this week that the Administration did not support regulation of carbon dioxide as an air pollutant under the Clean Air Act; the position reflects one of our central guiding principals. Over the last eight years, a number of environmental and energy policies were adopted that placed enormous constraints on the continued viability of coal-based generation. The recent price volatility and reliability problems in our electricity and natural gas markets are symptomatic of a larger energy crisis in the United States and in part are the result of a loss of fuel diversity in our energy mix engendered by those policies.

Our coalition is committed to being part of the clean air solution by continuously improving the environmental performance of coal-based generation through increased public-private funding and incentives for development and deployment of advanced clean coal technologies. The group also seeks environmental policies that: 1) rely on sound science and demonstrable public health benefits, 2) consider fuel costs and security and reliability of electric supplies, 3) establish practical compliance schedules, 4) provide reasonable certainty for investments in environmental controls and new generating facilities; and 5) give states appropriate flexibility in implementing Clean Air Act policies.

Enclosed are a set of briefing papers covering the major issues that we have discussed with your Administration's representatives, including recommendations on establishing a robust, voluntary CO2 reduction program, reforming EPA's New Source Review process, establishing consistent NOx standards and timetables, and developing a more flexible and cost-effective Mercury rulemaking.

We look forward to working with you and other members of the Energy Policy Development Task Force to craft a balanced and effective energy policy for our nation.

Sincerely,

William T. McCormick, Jr.
Chairman and Chief Executive Officer
CMS Energy

Enclosure

cc: The Honorable Spencer Abraham
    The Honorable Donald Evans
    Mr. Lawrence Lindsey
    Mr. Andrew Lundquist

2267

DOE003-0911

Obtained and made public by the Natural Resources Defense Council, March/April 2002
THE NATIONAL MINING ASSOCIATION
AND
THE ASSOCIATION OF AMERICAN RAILROADS
MEMORANDUM OF UNDERSTANDING
IN REGARD TO RAILROAD COAL TRANSPORTATION

I. INTRODUCTION

The National Mining Association, hereinafter referred to as "NMA", the Association of American Railroads, hereinafter referred to as "AAR", and those members of the AAR and the NMA who have subscribed to this memorandum of understanding express their mutual agreement and acceptance of the Rail/Coal Communication/Dispute Resolution Process, which is set forth herein.

NMA and AAR realize that abundant coal reserves mined in the United States represent a strategic resource required to fuel the generation of electricity and to furnish an important feedstock for other purposes, and that U.S. coal exports are significant contributors toward improving the U.S. balance of trade with other countries that are coal consumers.

NMA and AAR recognize that the coal industry must rely on dependable, efficient railroad services for distribution of coal produced in the eastern and western states, and that coal traffic represents a highly important element of total railroad freight carried by the railroads and is important to the economic health of the railroads.

NMA and AAR further recognize that the rail industry must rely upon a reliable and adequate supply of coal, equipment and mining infrastructure in order to provide railroad coal customers with efficient service.
II. PURPOSE

This agreement by and between NMA and AAR is entered into for the purpose of establishing a Rail/Coal Communication/Dispute Resolution Process, which will seek inter-industry understanding and resolution of issues which may arise with regard to the adequacy and reliability of railroad and coal company services required for coal shipments from mines to power plants and other coal-consuming facilities, and to inland and coastal ports, in order to supply U.S. coal to domestic and foreign markets. The process will only consider matters which involve providing and utilizing transportation services for coal shipments, and will not discuss transportation rates, costs, or other charges for rail traffic services.

III. STRUCTURE

A. Joint Policy Committee

A Joint Policy Committee shall be created, comprised of six members consisting of the Chief Executive Officers ("CEO") of the NMA, the AAR, two members of the AAR (to be designated by the AAR), and two members of the NMA (to be designated by the NMA). It shall meet annually, or at any other time, at the request of a member of the Committee, to discuss policy issues of industry-wide application relating to the rail transportation of coal. The CEOs of all other AAR and NMA members will also be invited to attend and fully participate in the annual Committee meeting. The Joint Policy Committee shall not have authority to set rates or charges or reach any agreement relating to rate related matters. The annual meetings will be alternately hosted by the AAR and the NMA.
B. Joint Coal Logistics Committee

A Joint Coal Logistics Committee shall be created, comprised of ten members consisting of four railroad coal marketing vice presidents (to be designated by the AAR), four vice presidents of members of the NMA who are responsible for rail transportation within their respective organizations (to be designated by the NMA), and one representative each from the AAR and the NMA. It shall meet semi-annually, or at any other time, at the request of a member of the Committee, to examine, and if applicable, make non-binding recommendations regarding industry-wide issues relating to rail transportation service, efficiency and deployment of assets. The Joint Coal Logistics Committee shall not have authority to set rates or charges or reach any agreement relating to rate related matters. Each semi-annual meeting will be scheduled to allow for in-depth examination of rail coal transportation issues. The meetings will be alternately hosted by the AAR and the NMA.

The Joint Coal Logistics Committee will elect a chairman from its members. The chairman, in alternate years, will be a member of the NMA delegation or the AAR delegation serving on the Committee. The presidents of NMA and AAR will identify matters for consideration by the Committee during its semi-annual or special meetings. The Committee will act as an advisory body only, with the view of providing professional expertise on matters it considers, and of communicating with the association presidents and the Joint Policy Committee on methods for improving both rail service and coal supply reliability and adequacy to overcome problems that may arise with regard to coal shipments on a nationwide or a regional venue.
IV. DISPUTE RESOLUTION PROCESS

A. In the event of disputes between a member of the AAR and a member of the NMA who subscribe to this agreement, those members consent to participate in a dispute resolution process. The goal of this process will be to enable the parties to develop a voluntary, mutually acceptable resolution to their dispute.

B. In the event of disputes, prior to invoking this dispute resolution process AAR and NMA members subscribing to this agreement agree to employ their best efforts to resolve differences through expanded communications and good faith negotiations between the parties involved.

C. If mutual discussions between AAR and NMA members who have subscribed to this agreement do not result in dispute resolution, both parties shall advise the CEOs of their respective organizations of their difficulties. Either CEO may then submit a written request to the CEOs of both the AAR and the NMA to review the dispute.

D. Upon receipt of a request for review, the CEOs of the AAR and the NMA will initiate the following dispute resolution process.

1. Step 1. Convene a panel consisting of the CEOs of the AAR, the NMA and a representative of each organization involved in the dispute. The dispute resolution shall be conducted via informal non-binding meeting or meetings among the panel members in which they will seek resolution of the dispute.

2. Step 2. If the dispute cannot be resolved by the panel convened in Step 1, and if both association CEOs agree, then the matter will be presented to a panel consisting of the
CEOs of the companies involved and the association CEOs. This meeting will seek to develop a consensus on recommended actions among the participants.

E. The dispute resolution process shall be continued until the matters in dispute are resolved or the panel members make a finding that there is no possibility of settlement through the dispute resolution process. All matters relating to a dispute resolution process involving a specific dispute shall be treated as confidential, including the convening of a panel to review such dispute. No party to the process shall disclose to the public that a dispute resolution process is ongoing. Statements, notes, and all records associated with the dispute resolution process shall be treated as confidential and privileged against use in any other proceeding relating to the dispute. Any notes taken by persons during the process shall be destroyed at the conclusion of the process, except for the notes of any final agreement reached by the parties.

V. TERM

This memorandum of understanding shall be effective as of the date executed by both the NMA and the AAR and shall remain in effect through and including December 31, 2000.
The parties agree to the policies, principles and procedures stated herein. Individual members of the NMA and the AAR will indicate their acceptance of this memorandum of understanding by executing a separate document indicating their agreement to subscribe to and be bound by the terms and conditions of this memorandum of understanding.

NATIONAL MINING ASSOCIATION ASSOCIATION OF AMERICAN RAILROADS

[Signatures]

12/1/99
Western Independent Refiners Association
Impacts of EPA Regulation

Small Refiners Are Key

- WIRA represents refiners with fewer than 1,500 employees and less than 155,000 barrels per day total capacity. WIRA members produce a full slate of petroleum products including everything from gasoline, diesel and jet fuels to asphalt, lube oil and specialty petroleum products.
- Today, approximately 124 refineries are operating in this country. About 25 percent are small, independent refiners. Small business refiners are primarily owned by U.S. citizens, including privately held businesses and one farmer cooperative.
- Small independent refiners employ thousands of people and each company pays millions of dollars in taxes, even after excluding income taxes.
- In addition to maintaining competition, small and independent refiners often supply other petroleum products not otherwise available in certain areas. For example, small refiners manufacture 100 percent of California’s grade 80-aviation fuel, aliphatic solvents, and JP-4 jet fuel. Small refiners also manufacture 100 percent of the asphalt produced in southern California and much of the off-road diesel fuel. Half of the diesel fuel produced in the San Joaquin Valley, California’s farm belt, is refined by small refiners.

Refining Capacity is at a Maximum

- As Secretary of Energy Spencer Abraham noted in recent comments to the United States Chamber of Commerce, the number of American refineries has been cut in half since 1980. Many of these were small business refiners unable to meet the challenges of poor refining margins and expensive regulations. Meanwhile, no new refinery has been built in the United States in over 25 years and regulatory requirements limit the ability of existing refineries to expand capacity.
- Government regulations require the production of more than 15 types of gasoline. Existing refineries are operating at capacity resulting in more frequent unplanned shutdowns. Every small refiner forced from the marketplace increases our vulnerability. Given the foregoing, one must agree with Secretary Abraham that we “have a refining industry strained to capacity, leaving us dangerously vulnerable to regional supply disruptions and price spikes.”

Federal Regulations Burden Small Refiners Disproportionately

- On January 18, 2001, the EPA published new regulations, which create new standards for levels of sulfur in highway diesel fuel beginning in June 2006. Under the new regulations, refiners must meet a stringent new standard of 15 parts per million sulfur limit for most on-road diesel volume (“Ultra Low Sulfur Diesel Fuel”).
- Small refiners produce about four percent of the Nation’s diesel fuel and in some regions produce over half of the diesel fuel.
• Access to crude oil is an ongoing challenge, as large companies merge and the remaining mega-companies are not consistently willing to supply small refineries.

• Wastewater treatment controls and stationary source air quality controls have become increasingly stringent, thus raising costs for small refineries.

The challenges facing small refineries continue. Not only must they compete head to head with some of the largest companies on the planet, but also they must comply with increasingly stringent government regulations. Of most concern: on January 18, 2001, the EPA published new regulations, which create new standards for levels of sulfur in highway diesel fuel beginning in June, 2006. Under the new regulations, refineries must meet a stringent new standard of 15 parts per million sulfur limit for most on-road diesel volume (“Ultra Low Sulfur Diesel Fuel”). Small refineries produce about four percent of the Nation’s diesel fuel and in some regions produce over half of the diesel fuel. In the final rule, EPA stated regarding the diesel sulfur standards “that small business refineries would likely experience a significant and disproportionate financial hardship in reaching the objectives of our diesel fuel sulfur program.” In the final rule, EPA agreed with the final Small Business Administration report regarding the diesel sulfur standards “that small business refineries would likely experience a significant and disproportionate financial hardship in reaching the objectives of our diesel fuel sulfur program.”

However, EPA has made no provision to assist small business refineries in financing the mandated capital expenditures.

The new regulations also will make it even less likely that new refineries will ever be built. With the exception of one small topping facility in Alaska, no new refinery has been built in the United States for almost 20 years. Existing facilities are operating at full sustainable capacity. Operational demands imposed by the new regulations will result in a reduction of on-road diesel production. At the same time, U.S. consumer demand for diesel fuel, as forecast by the Energy Information Administration, is expected to grow by 6.5 percent between now and 2007. If small business refineries are eliminated from diesel production, supply shortages will become even more likely. Therefore, it is important to seek methods to reimburse small business refineries for their costs in meeting these new government imposed mandates, which endanger their long-term economic viability.

EPA estimates that small business refineries will incur average capital costs of $14 million per facility to meet the new diesel regulations. For some facilities, the cost will be substantially more.

In addition, costs to produce low-sulfur gasoline and to comply with other regulations will add significantly to capital requirements in approximately the same time frame. Such capital investments are significantly beyond the financial capability of facilities operated by small business refineries, whose total investment is dwarfed by these requirements. On top of the initial required capital expenditures, the related increases in operating costs could equal or exceed the refineries’ historical annual profits, and thus, imperil the viability of these important US businesses.

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Obtained and made public by the Natural Resources Defense Council, March/April 2002
While WIRA does not oppose the regulation, and is fully committed to compliance, we believe that national energy policy should take into account the importance of the small refiners and should include proposals for mitigating the impact of this regulation. Without such provisions, some small business refiners will shut down and all will struggle to meet the mandated expenditures. Such a policy ignores the important role of the small business refiner in the U.S. energy market. The result of such a policy will have serious consequences for our country.

Conclusion: U.S. Government Energy Policy Should Recognize the Role of the Small Refiner

The challenges to small business refiners, including the need for mitigation for the impact of otherwise appropriate environmental policies, should be recognized by the Congress and should be addressed in overall U.S. energy policy. If this does not occur, and small refiners go out of business, the competitive fabric of the U.S. oil and gas industry will be irreparably damaged.

Thank you for your consideration of these important comments.
STATEMENT OF CRAIG MOYER, MANATT, PHELPS & PHILLIPS
SUBMITTED ON BEHALF OF
THE WESTERN INDEPENDENT REFINERS ASSOCIATION
BEFORE THE HOUSE SUBCOMMITTEE ON ENERGY AND AIR QUALITY
MARCH 30, 2001

On behalf of the Western Independent Refiners Association (WIRA), in my
capacity as counsel for WIRA, I am pleased to provide this statement for the record
providing an overview of the current challenges facing small business refiners (refiners
with fewer than 1500 employees and less than 155,000 barrels per day total capacity).
WIRA is a trade association of small and independent refineries on the West Coast. At
this time, ten small independent refineries continue to operate on the West Coast, nine in
California and one in Tacoma, Washington. In California, these refineries are located in
each of the three refining areas within California. One is located in the San Francisco
Bay area. One is located in the Bakersfield area of the Southern San Joaquin Valley and
the remaining facilities operate in the Los Angeles Basin. Small independent refineries
employ thousands of people and each company pays millions of dollars in taxes, even
after excluding income taxes. WIRA members produce a full slate of petroleum products
including everything from gasoline, diesel fuel and jet fuel to asphalt, lube oil and
specialty petroleum products. At this time, when it is clear that all domestic energy
sources should remain viable and that no domestic source should be overlooked, I believe
that it is important for this Subcommittee to understand the role of small refiners to the
energy supply of our nation.

The Pro-competitive Role of the Small Refiners

Small and independent refiners have long been recognized as an important
competitive force in the refining sector. Individually, each small refiner represents a
relatively small share of the petroleum product marketplace. Cumulatively, however,
their impact is substantial. Their pricing competition pressures the larger integrated
companies to lower prices to the consuming public. Without that competition pressure,
consumers will pay more. For example, in early 1991, Amoco shut down a 40,000 barrels
per day refinery in Casper, Wyoming, and gasoline prices jumped almost 10 cents per
gallon. In California, the Attorney General concluded that after five small refiners shut
down because they could not manufacture California's cleaner burning gasoline, the loss
of competition cost consumers hundreds of millions of dollars. Through experience, we
know that when small refiners leave the marketplace, prices go up and consumers suffer.

Congress and many agencies, including the Environmental Protection Agency
("EPA") and the California Air Resources Board ("CARB"), have long recognized the
importance of the independent refining sector to maintaining a competitive market for
petroleum products. For example, after EPA promulgated rules limiting the sulfur
content of diesel fuel to 500 parts per million effective October 1, 1993, Congress
recognized the implications of this rule on small diesel refiners and authorized the
issuance of acid rain credits to small diesel refiners pursuant to Section 410 (h) of the
1990 Clear Air Act amendments. Because of the important pro-competitive impact of small refiners, CARB, an agency that has promulgated perhaps the most stringent fuels regulations in the country, has provided separate treatment for small refiners in virtually every fuels regulation it has passed since 1988. In its two most recent fuels rulemakings, EPA has authorized separate treatment for small business refiners, as well. Even the South Coast Air Quality Management District, an agency leading the nation and perhaps the world, in stringent air quality regulations, authorized separate treatment for small refiners in its recently promulgated Rule 431.1 regulating diesel fuel.

In addition to maintaining competition, small and independent refiners often supply other petroleum products not otherwise available in certain areas. For example, small refiners manufacture 100 percent of California’s grade 80 aviation fuel, aliphatic solvents, and JP-4 jet fuel. Small refiners also manufacture 100 percent of the asphalt produced in southern California and much of the off-road diesel fuel. Half of the diesel fuel produced in the San Joaquin Valley, California’s farm belt, is refined by small refiners.

Small business refiners also fill a critical national security function. For example, in 1998 and 1999, small business refiners provided almost 20 percent of the jet fuel used by U.S. military bases. This adds up to almost 500 million gallons of jet fuel supplied each year under defense contracts between the government and small business refiners.

Challenges Facing the Industry

Today, approximately 124 refineries are operating in this country. About 25 percent are small, independent refiners. Small business refiners are primarily owned by U.S. citizens including privately held businesses and one farmer cooperative.

As Secretary of Energy Spencer Abraham noted in recent comments to the United States Chamber of Commerce, the number of American refineries has been cut in half since 1980. Many of these were small business refiners unable to meet the challenges of poor refining margins and expensive regulations. Meanwhile, no new refinery has been built in the United States in over 25 years and regulatory requirements limit the ability of existing refineries to expand capacity. Government regulations require the production of more than 15 types of gasoline. Existing refineries are operating at capacity resulting in more frequent unplanned shutdowns. Every small refiner forced from the marketplace increases our vulnerability. Given the foregoing, one must agree with Secretary Abraham that we “have a refining industry strained to capacity, leaving us dangerously vulnerable to regional supply disruptions and price spikes.”

Some of the major challenges facing small refiners in today's market include:

- Small refiners are large users of electricity and natural gas. The remarkably high prices of these inputs are affecting the small refiners.
- The phase out of MTBE as an oxygenate will lead to increased costs as reformulations are required.